ENFORCEMENT OF THE 2020 FINANCIAL INFORMATION PUBLISHED BY ISSUERS SUBJECT TO THE TRANSPARENCY LAW

Pursuant to the law of 11 January 2008 on Transparency requirements for issuers (the "Transparency Law"), the CSSF is monitoring that financial information published by issuers, in particular their consolidated and non-consolidated financial statements, is drawn up in compliance with the applicable accounting standards.

As issuers are now preparing their financial information for the 2020 fiscal year, the CSSF wishes to draw the attention of those issuers preparing their financial statements in accordance with the International Financial Reporting Standards, as well as of their auditors, to a number of topics and issues that will be the subject of a specific monitoring during its enforcement campaign planned for 2021.

1. European Common Enforcement Priorities

As in previous years, the European Securities and Markets Authority ("ESMA"), together with the European national accounting enforcers, including the CSSF, identified European common enforcement priorities (the "ECEPs") for the 2020 financial reports to which particular attention will be paid when monitoring and assessing the application of IFRS requirements. ESMA issued on 28 October 2020 a public statement which defines these ECEPs. This document is available on the CSSF website under Enforcement of financial information.

The 2020 ECEPs focus on the need to provide adequate transparency regarding the consequences of the COVID-19 pandemic, particularly in relation to the following standards:

- IAS 1 *Presentation of Financial Statements*;
- IAS 36 *Impairment of Assets*;
- IFRS 9 *Financial Instruments* and IFRS 7 *Financial Instruments: Disclosures*; and
- IFRS 16 *Leases*.

In its communication, ESMA also set priorities related to non-financial statements for the 2020 year-end:

- Impact of the COVID-19 pandemic on non-financial matters;
- Social and employee matters;
- Business model and value creation; and
- Risk relating to climate change.

In the coming weeks, the CSSF will also publish a specific statement dealing with the results of a thematic review carried out on the 2019 non-financial information disclosed by the issuers under its supervision as well as its expectations and recommendations in this field.

2. Points of attention identified by the CSSF

When establishing its enforcement campaign for next year, the CSSF considered the 2020 particular context in relation to the COVID-19 pandemic and has decided not to add other priorities than those identified at European level. Therefore, the CSSF intends to focus on the ECEPs and the related issues, already identified during its COVID-19 Thematic review performed in October 2020, that are considered as the most relevant for the issuers under its jurisdiction.

Thus, the CSSF's 2020 enforcement campaign will focus in particular on the following topics:

a. Impairment testing of non-financial assets

As highlighted in the COVID-19 Thematic review, the CSSF observed that the assessments made by management with regard to the recoverable value of non-financial assets did not always appear consistent with the impacts of the COVID-19 pandemic (on the first half-year 2020 and planned) described elsewhere in the financial reports.

The CSSF will be particularly vigilant in this regard and expects issuers to base their cash flow projections on reasonable and supportable assumptions when determining the value in use in the context of their annual impairment testing of non-financial assets.

In light of the increased uncertainties faced by issuers during the period, issuers should update any assumptions used in previous interim periods to reflect the latest available information and evidence. Use of multiple scenarios is encouraged in order to better assess the recoverable values despite the uncertainties related to the COVID-19 crisis.

The CSSF also expects issuers to disclose adequate and detailed information on the estimates and key assumptions used. Moreover, the CSSF reminds that issuers should disclose the sensitivity analysis as required by IAS 36 and take into account that, due to the current uncertain environment, the range of reasonably possible changes in key assumptions may be larger than usual.

The CSSF intends to monitor impairment tests performed by issuers concerned and will ensure that disclosures provide relevant information to the users of the financial statements.

b. Change in credit risk and expected credit losses

On top of ESMA considerations related to the application of IFRS 9 *Financial instruments* and IFRS 7 *Financial instruments – Disclosure* in the ECEPs public statement, the CSSF highlights the need for corporates to adjust the measurement and disclosure of impairment of trade receivables to the current uncertain environment.

Commission de Surveillance du Secteur Financier

Whereas the determination of loss rates and measurement of expected credit losses (ECL) may usually not involve significant judgement for most corporates, the current context of high economic uncertainty has changed the situation. The CSSF reminds issuers that when assessing impairment, they should consider reasonable and supportable information, including available forward-looking information.

The CSSF will scrutinise the disclosures related to ECL and expects issuers to provide specific information on how they have incorporated the effects of the COVID-19 crisis into their ECL model estimates, including relevant changes in their credit risk management practices.

c. Fair value measurement of investment properties

Due to the disruption to the market caused by the COVID-19 pandemic, there are substantially more uncertainties than normal and therefore a higher risk that the assumptions upon which issuers have based their investment properties valuations might finally need to be reassessed. Indeed, the fair value of investment properties must reflect market participants' views and market data at the measurement date under current market conditions. There may be an increase in the amount of subjectivity involved in fair value measurements, especially those based on unobservable inputs (Level 3).

The CSSF reminds that under IFRS 13 *Fair value measurement*, an entity should apply valuation techniques consistently. A change in valuation technique or its application is appropriate if the change results in a fair value measurement that is equally or more representative of fair value under the circumstances. Changes in market conditions is an example of such a change.

In such circumstances, the CSSF will particularly ensure that the requirements of IFRS 13 are well respected by issuers when determining the fair value of their investment properties.

Finally, IFRS 13 deals with uncertainty in relation to Level 3 fair value measurements through providing users with appropriate disclosure. For example, including a description of the valuation techniques used, how decisions are made in relation to valuation procedures and the sensitivity of fair value measurements to significant unobservable inputs.

The CSSF will also pay close attention to these disclosures and will ensure that concerned issuers provide useful and meaningful information for the users of financial information, covering in particular the significant judgements and the major sources of estimation uncertainty.

Commission de Surveillance du Secteur Financier

d. Recognition and measurement of deferred tax assets

Another point of attention identified by the CSSF concerns the recognition and measurement of deferred tax assets. The current challenges and effects of the COVID-19 pandemic impact issuers' operations. Many governments have granted relief and support measures. Both uncertainties and such specific measures may affect issuers' projections of future taxable profits that are used to assess the recoverability of deferred tax assets.

Indeed, in such circumstances, an issuer's projections of future taxable profits may be affected by, amongst others:

- changes in forecasted cash flows;
- changes in a company's tax strategies, including profits distribution or repatriation; and
- changes to the income tax law introduced as part of a government's measures in response to COVID-19 – e.g. tax reliefs for certain types of income, additional tax deductions, a reduced tax rate or an extended period to use tax losses carried forward.

When preparing projections of future taxable profits for the purposes of the deferred tax asset recognition test, an issuer needs to reflect expectations at the reporting date and use assumptions and judgements that are consistent with those used for other recoverability assessments – e.g. impairment testing of non-financial assets.

The CSSF also reminds issuers to consider the ESMA Public Statement setting out expectations regarding the application of the requirements in IAS 12 *Income taxes* relating to the recognition, measurement and disclosure of deferred tax assets arising from unused tax losses, as well as IFRIC 23 *Uncertainty over Income Tax Treatments* which applies to the determination of taxable profit (tax loss), tax bases, unused tax losses, unused tax credits and tax rates, when there is uncertainty over income tax treatments.

In this respect, the CSSF will analyse the recoverability of deferred tax assets recognised in this particular situation and will focus on the information provided by issuers in relation to the nature of the evidence supporting the recognition of deferred tax assets when the utilisation of the recoverability of the asset is dependent on future taxable profits, as required by paragraph 82 of IAS 12.

More information on inspections and findings by the CSSF within the framework of its mission under Article 22 (2) h) of the Transparency Law are given under Enforcement of financial information and in its annual report.